

**SUPPLEMENTAL STATEMENT
NATURAL GAS
ILL. C.C. NO. 17**

Filed with the Illinois Commerce Commission on February 25, 2009

North Shore Gas Company ("North Shore Gas"), for the reasons discussed briefly further below and shown in its submissions, proposes an increase in its rates for gas distribution service and several new rate mechanisms. The total amount of the requested revenue increase (the revenue deficiency) is \$21,986,000.

North Shore Gas was last granted a rate increase in 2008, in Illinois Commerce Commission ("Commission") Docket Nos. 07-0241/07-0242 (cons.). That rate case was based on a historical test year of September 30, 2006. In contrast, this rate filing is based on a forward looking test year ending December 31, 2010. The significant changes that have occurred over these four years are attributable to several factors. First, Mains and Services Expense and Other Distribution and Storage Expense, which are non-capitalized costs incurred to operate and maintain North Shore Gas' underground distribution system, have increased. This increase is generally attributable to increased costs resulting from the transmission pipeline integrity program, additional head count, and increased transportation costs. Second, System Capital Investment, which is the return on and return of capital invested since the prior rate case, has increased due to North Shore Gas' ongoing significant investment in its distribution system.

Third, Cost of Capital, which represents the increased costs of long-term debt and common equity for North Shore Gas since the last rate case, has increased. The overall cost of capital is the required return on the investment of North Shore Gas (net of depreciation) in its assets, primarily distribution pipe. In order to attract capital for new investments, existing investors must receive an adequate return on their investment. The events that have shaken the financial markets since the last rate case have, among other things, increased the cost of capital for businesses throughout the world and North Shore Gas is no exception. Fourth, costs related to Administrative and General and Customer Accounts, including billing, collection, call center, as well as support functions such as human resources, finance and accounting, information systems, have increased. The primary drivers in the increases to these costs are inflation and increased administrative requirements. Finally, Pensions and Benefits have increased due to inflation and increased service costs.

Without this rate filing, North Shore Gas will not be able to recover its cost of service, which would result in earning a return on equity of 1.1% in 2010, less than what the Commission just approved last year in North Shore Gas' last rate case. North Shore Gas is requesting a rate of return on its rate base of 9.18%. Further, North Shore Gas is also proposing three new Riders,

Rider UEA, Uncollectible Expense Adjustment; Rider FCA, Franchise Cost Adjustment; and Rider GCA, Governmental Agency Compensation Adjustment. If approved, Rider UEA will enable North Shore Gas to better recover the gas costs related uncollectible accounts expenses while Riders FCA and GCA will allow proper allocation of costs generated by a governmental entity to those customers who reside within the boundaries of the entity's geographic area.

**SUMMARY OF PREPARED DIRECT TESTIMONY
IN SUPPORT OF NORTH SHORE GAS' FILING**

North Shore Gas' filed tariffs are supported by the testimony of witnesses from within North Shore Gas as well as independent experts. The testimony submitted with the filing are as follows:

- James F. Schott, Vice President – Regulatory Affairs, Integrys Energy Group, Inc. and North Shore Gas (North Shore Ex. JFS-1.0), provides an overview of the reasons North Shore Gas finds it necessary to request a rate increase at this time. He also summarizes the reasons for rate design and tariff changes in this filing, including rider proposals. Finally, Mr. Schott identifies each of the other witnesses providing direct testimony in support of North Shore Gas' tariffs.
- Christine M. Gregor, Director, Operations Accounting, North Shore Gas (North Shore Ex. CMG-1.0), presents the operating income statement for the forecasted calendar test year 2010, including projected costs. She discusses variances in operating expenses from the test year to 2007. Ms. Gregor also discusses the methodology used in the preparation of the operating income statement for the test year, certain ratemaking adjustments, and certain compliance matters.
- Sharon Moy, Rate Case Consultant, Integrys Business Support (North Shore Ex. SM-1.0), addresses the test year revenue requirement, operating income and expenses, the adjustments to operating income and expenses, and the Gross Revenue Conversion Factor.
- David W. Clabots, Manager, Sales and Revenue Forecasting, Integrys Business Support (North Shore Ex. DWC-1.0), explains how the customer demand forecast was derived for the 2010 test year. He also compares demand between North Shore Gas' forecasted 2010 test year and North Shore Gas' last historical year (2008) (using six months of actual results).
- Michael A Small, Assistant Controller of Financial and Accounting Services, Integrys Business Support (North Shore Ex. MAS-1.0), addresses the effects of various affiliated interest agreements on North Shore Gas' revenue requirement.
- Paul R. Moul, Managing Consultant, P. Moul & Associates (North Shore Ex. PRM-1.0), addresses the required rate of return on common equity for North Shore Gas.
- Bradley A. Johnson, Treasurer, North Shore Gas (North Shore Ex. BAJ-1.0), addresses the capital structure and cost of capital (its overall required rate of return on its investments) for North Shore Gas.

- Valerie H. Grace, Manager, Gas Regulatory Services, Integrys Business Support (North Shore Ex. VG-1.0), addresses and supports the proposed rate design for North Shore Gas and the three new riders North Shore Gas is proposing, Rider UEA, Rider FCA and Rider GCA. She also addresses and supports changes to the Schedule of Rates for Gas Service for North Shore Gas.
- Brian M. Marozas, Manager, Planning, Modeling and Contract Administration, Integrys Business Support (North Shore Ex. BMM-1.0), explains how he developed the forecast of normal heating degree days for North Shore Gas using an historical 12 year average.
- John Hengtgen, Rate Case Consultant, Integrys Business Support (North Shore Ex. JH-1.0), describes the rate base, adjustments to rate base, and the cash working capital components of the request of North Shore Gas for a general increase in rates.
- John J. Spanos, Vice President, Valuation and Rate Division, Gannett Fleming, Inc. (North Shore Ex. JJS-1.0), presents North Shore Gas' new depreciation study.
- Joylyn C. Hoffman Malueg, Rate Case Consultant, Integrys Business Support (North Shore Ex. JCHM-1.0), describes North Shore Gas' embedded cost of service study for the 2010 future test year used by Ms. Grace in her testimony to support the proposed changes in the North Shore Gas rate schedules.
- Edward Doerk, Vice President Gas Operations, North Shore Gas (North Shore Ex. ED-1.0), addresses certain major additions to rate base since the last test year. Mr. Doerk also describes North Shore Gas' forecasted capital investments.

SCHEDULE OF RATES FOR GAS SERVICE

North Shore Gas has filed proposed changes to its Schedule of Rates for Gas Service, ILL. C.C. No. 17, effecting a general increase in rates and revising other terms and conditions. A complete list of the tariff sheets that have been revised is included in the letter of transmittal submitted with the filing of the tariffs in accordance with 83 Ill. Adm. Code Part 255.

CHANGES TO SERVICE CLASSIFICATIONS AND MISCELLANEOUS CHARGES

The objectives of North Shore Gas' proposed changes to its Service Classifications and miscellaneous charges are (1) recover North Shore Gas' revenue requirement, (2) better align revenues with underlying costs, (3) send the proper price signals, (4) provide more equity between and within rate classes, (5) maintain rate design continuity, (6) reflect gradualism and (7) retain customers on North Shore Gas' system. The principal changes proposed by North Shore Gas include the following:

- S.C. No. 1, Small Residential Service, will be revised to set different customer charges for sales and transportation customers rather than different distribution charges for such customers as rates are presently set. The monthly customer charge will increase for both sales and transportation customers.

- S.C. No. 2, General Service, will be revised to expand the number of meter classes from two to three. Further, the monthly customer charges for S.C. No. 2 will increase. Finally, an eligibility requirement will be imposed on these customers.
- S.C. No. 3, Large Volume Demand Service, will be revised to change all charges. Further, the demand charge, which under present rates is a declining block rate structure, will be set at a flat charge on a per demand therm basis. Finally, these customers will no longer be required to sign a contract.
- S.C. No. 5, Standby Service, will be eliminated and all customers served under this classification will be transferred to S.C. No. 2. As a result, any references to S.C. No. 5 will be removed.
- Service reconnection and service activation charges will be changed.
- For the Second Pulse Capability, a February 14, 2008 grandfathering date will be added so that the language remains accurate after the effective date of the tariff sheet charges.
- Language for Correction for Pressure, Temperature and/or Supercompressibility is revised so that it is consistent with North Shore Gas' practices concerning the pressure at which customers are served.
- A definition of "person" will be added related to the changes proposed to Riders 4 and 5.

A detailed description of the proposed changes to North Shore Gas' Service Classifications, Terms and Conditions of Service, and miscellaneous charges is provided in the prepared direct testimony and accompanying exhibits of North Shore Gas witness Ms. Grace, Manager, Gas Regulatory Services (North Shore Ex. VG-1.0). A comparison of North Shore Gas' present and proposed rates can be found on North Shore Exhibit VG-1.4 accompanying Ms. Grace's testimony.

CHANGES TO RIDERS AND PROPOSED NEW RIDERS

North Shore Gas is proposing the following changes to its existing Riders:

- Rider 2 (Gas Charge) will be revised to eliminate references to S.C. No. 5, and the transitional transportation tariffs.
- Rider 4 (Extension of Mains) and Rider 5 (Service Pipe) will be revised to address situations where a requestor for a main or service is a person or a group of persons, who are developing the property for eventual gas service.

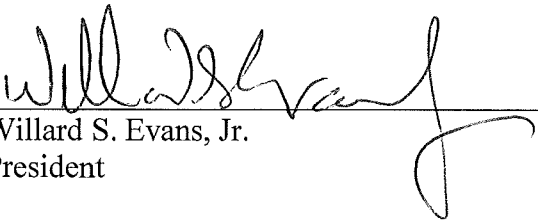
In addition, North Shore Gas is proposing three new Riders, Riders UEA (Uncollectible Expense Adjustment), Rider FCA (Franchise Cost Adjustment), and Rider GCA (Governmental Agency Compensation Adjustment):

- Rider UEA is designed to recover gas costs related Account No. 904 Uncollectible Accounts expenses through a factor that will be applied to customer bills rather than through base rates.

- Rider FCA will recover the costs of reduced rate service or monetary contribution provided by North Shore Gas solely from those customers residing in each local governmental unit receiving such rate or contribution.
- Rider GCA would recover fees and costs that North Shore Gas incurs as a result of requirements that a local governmental unit imposes on North Shore Gas solely from those customers taking service from North Shore Gas within the boundaries of each local governmental unit imposing such costs.
- Rider FST-T (Full Standby Transportation Transition Service) will be eliminated and any reference to this rider will be eliminated.
- Rider SST-T (Selected Standby Transportation Transition Service) will be eliminated and any reference to this rider will be eliminated.
- Rider LST-T (Large Volume Selected Standby Transportation Transition Service) will be eliminated and any reference to this rider will be eliminated.
- Rider TB-T (Transportation Balancing Transition Service) will be eliminated and any reference to this rider will be eliminated.
- Rider P-T (Pooling Transition Service) will be eliminated and any reference to this rider will be eliminated.
- Riders FST (Full Standby Transportation) will be revised to reduce the Administrative Charge. It also will be revised to remove the effective date. Revisions will be made to show that certain therm calculations are rounded to the nearest 10 (*i.e.*, to the nearest dekatherm).
- Rider SST (Selected Standby Transportation) will be revised to reduce the Administrative Charge. It also will be revised to remove the effective date. Revisions will be made to show that certain therm calculations are rounded to the nearest 10 (*i.e.*, to the nearest dekatherm).
- Rider P (Pooling) will be revised to reduce the Pooling Charge. It also will be revised to remove the effective date.
- Rider AGG (Aggregation Service) will be revised to result in an Aggregation Charge credit rather than a charge. It also has been revised to show that certain therm calculations are rounded to the nearest 10 (*i.e.*, to the nearest dekatherm).

Detailed descriptions of all of the above-referenced changes and additions to riders are provided in the prepared direct testimony and accompanying exhibits of Ms. Grace.

NORTH SHORE GAS COMPANY



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